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SUPREME COURT, U. S.

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IN THE

SUPREME COURT OF THE UNITED STATES

_____ Term, [redacted] 1968

No. 1336

In the Matter of:

LECKIE FREEBURN COAL COMPANY - Bankrupt

OCTAVIA FOSTER,
BILLY HOWARD SMITH,
CLYDE HEFLIN, Trustee,
ETHEL SMITH and
JUDY PORTER - - - - - - - - Petitioners

Versus

WILLARD M. HAMBLIN, Trustee in Bankruptcy - - - - - - - - - - Respondent

PETITION FOR WRIT OF CERTIORARI

To the United States Court of Appeals for the Sixth Circuit

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LECKIE FREEBURN COAL COMPANY - - - *Bankrupt*

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VERSUS

WILLARD M. HAMBLIN, Trustee in
Bankruptcy - - - - - - - - - - *Respondent*

PETITION FOR WRIT OF CERTIORARI TO
The United States Court of Appeals for the Sixth Circuit

TO THE HONORABLE,
THE CHIEF JUSTICE AND
ASSOCIATE JUSTICES OF THE
SUPREME COURT OF THE UNITED STATES:

Octavia Foster, Billy Howard Smith, Clyde Heflin, Trustee, Ethel Smith and Judy Porter, the petitioners herein, pray that a writ of certiorari issue to review the Opinion and Judgment of the United States Court of Appeals for the Sixth Circuit, entered in the above entitled case on January 29, 1969.

OPINIONS BELOW

The Opinion of the United States Court of Appeals is unreported and is printed in Appendix A hereto.

JURISDICTION

The Judgment of the Circuit Court of Appeals was entered on January 29, 1969. The jurisdiction of the Court is invoked under 28 U. S. C. 1254 (1), and certiorari is sought pursuant to Rule 19 (b) of the rules of practice of the Supreme Court of the United States.

QUESTION PRESENTED

Under Kentucky law where a mineral lessor, by contract, obtains a lien upon the property and equipment of the lessee on the premises to secure the performance of the obligations of the lease and the payment of the royalties thereunder, to be valid as against creditors, must such mineral lease be physically recorded both as an instrument affecting realty and as an instrument affecting chattels under the Uniform Commercial Code, or under Kentucky Law is simply presenting such an instrument to the proper recording office sufficient to give notice to creditors and thus superiority to a trustee in bankruptcy representing their interest?

STATUTES INVOLVED

"KRS 382.110 RECORDING OF DEEDS AND MORTGAGES, PLACE OF RECORDING; CONTENTS OF DEED.

(1) All deeds, mortgages and other instruments required by law to be recorded to be effectual against purchasers without notice, or *creditors,*

shall be recorded in the county clerk's office of the county in which the property conveyed, or the greater part thereof, is located." (Emphasis ours.)

"KRS 382.080 RECORDING OF CONVEYANCE FOR LONGER THAN FIVE YEARS AND OF MARRIAGE AGREEMENT.

(1) No deed conveying any title to or interest in real property, or lease of oil, gas, *coal or mineral right and privilege, for a longer time than five years* nor any agreement in consideration of marriage shall be good against a purchaser for a valuable consideration without notice thereof, or any creditor unless the deed is acknowledged by the party who executed it, or is proved and lodged for record in the proper office as required by law." (Emphasis ours.)

"KRS 382.200 CROSS-INDEX OF REAL PROPERTY CONVEYANCES: FILING AND RECORDING PERSONAL PROPERTY INTERESTS.

(1) Except as provided in Subsection (2) of this section, each county clerk shall make and keep an alphabetical cross-index of all conveyances recorded in his office, and when a mortgage or deed of trust, or any other conveyance, *or contract* is lodged, in his office for record, he shall, at once, and before attending to any other business, place the names of the parties to the instrument upon the cross-index in his office, and shall within six days thereafter record the instrument.

(2) Chattel mortgages, financing statement or security agreements shall be filed and recorded in the manner set out in KRS 355.9-403." (Emphasis ours.)

UNIFORM COMMERCIAL CODE

"KRS 355.9-401 PLACE OF FILING; ERRONEOUS FILING; REMOVAL OF COLLATERAL.

(1) The proper place to file in order to perfect a security interest (on chattels) is as follows: (b) When the collateral is goods which at the time the security interest attaches are or are to become fixtures, then in the office where a mortgage on the real estate concerned would be filed or recorded; (c) In all other cases .... if the debtor is not a resident of this state but has a principal place of business in this state, in the office of the county court clerk in the county where the non-resident has a principal place of business. ...."

"KRS 355.9-403 WHAT CONSTITUTES FILING; ... (1) Presentation for filing of a financing statement and tender of the filing fee or acceptance of the statement by the filing officer constitute filing under this article."

See also: APPENDIX "B".

STATEMENT

The Bankrupt, Leckie Freeburn Coal Company, filed its voluntary petition in bankruptcy in the United States District Court for the Eastern District of Kentucky. Among the creditors filing claims were the petitioners herein who, as lessors, of the bankrupt, asserted a lien on equipment and supplies of the bankrupt pursuant to the provisions of a coal mining lease which granted the lessors a lien on all of the equipment and property of the bankrupt to secure the payment of the rents and royalties reserved. This lease, immediately subsequent to its execution, was

delivered to the Office of the County Clerk of Pike County and recorded by that office in the deed books of that county. The Clerk neither indexed it, nor recorded it in another section of the same office as an instrument affecting chattels, although the lease as executed met all the formal requirements as a document affecting chattels under the Uniform Commercial Code.

It is undisputed that at the time of the bankruptcy the bankrupt corporation was indebted to the lessors in the sum of $43,283.14.

The trustee in bankruptcy resisted this claim as a secured claim contending that as it had neither been recorded nor indexed as an instrument affecting chattels, under the Uniform Commercial Code, it was not notice to the creditors nor binding upon the trustee in bankruptcy.

The case was decided in the District Court and in the Circuit Court of Appeals on the very narrow issue that to be effective notice to creditors under Kentucky Law, the lease as it undertook to grant a lien on the chattels of the bankrupt was required to be *indexed* and *physically recorded* as an instrument affecting chattels under the Uniform Commercial Code.

The Circuit Court of Appeals adopted this position affirming the District Court even though in the course of its Opinion it admitted;

> "This Court is cognizant of the long line of property cases cited by appellant which seem contrary to this Court's position, but also notes that none of them relate to decisions under the Uniform Commercial Code."

REASONS FOR GRANTING THIS WRIT

The decision of the United States Court of Appeals for the Sixth Circuit invalidates, or places in jeopardy the lessors' liens in thousands of mineral leases affecting hundreds of thousand acres of mineral lands within the Commonwealth of Kentucky. As conceded by the Court in its Opinion, it is contrary to every reported decision of the Court of Appeals of Kentucky, and although the Court notes in its Opinion that none of these cases cited have been decided since the enactment of the Uniform Commercial Code, nevertheless those older cases relate to an issue that was so well settled as not to merit contention.

By the settled Law of Kentucky, a party recording an instrument simply leaves it with the clerk of the proper county and it is considered lodged for all purposes, even though the Clerk fails to record it, fails to index it, or fails in any other regard to do his duty. Even under the Uniform Commercial Code an instrument is filed by delivering it to the clerk when the clerk accepts it.

Illustrative of these cases are the following:

Webb v. Austin, 58 S.W. 808 holding the act of lodging was complete even though the mortgage was never recorded in any book.

Smith v. Chapman, 153 Ky. 70, 154 S.W. 915, where the Clerk failed to properly index a deed, it was held to be notice.

In Great Western Petroleum Corporation v. Samson, 192 Ky. 814, 234 S.W. 727, the Court held a gas and oil lease properly recorded even though the Clerk failed to index the instrument at all.

In Elkhorn Coal Corporation v. Hite, 225 Ky. 735, 9 S.W. 2d 1083, the Court held a deed which had been lodged for record, but improperly copied by the Clerk, constituted constructive notice.

In Seat v. Louisville and Jefferson County Land Company, 219 Ky. 418, 292 S.W. 968, the Kentucky Court held a property owner had constructive notice of the restrictive covenants contained on a plat of a sub-division which was not indexed by the Clerk.

In Carter Guaranty Company v. Cumberland and Manchester Railway Company, 219 Ky. 207, 292 S.W. 812, the Kentucky Court held that a chattel mortgage would be properly filed when delivered to the clerk even though the clerk failed to record it.

The enactment of the Uniform Commercial Code did not in any substance change the statutory requirements for recording chattel instruments in Kentucky. The pre-UCC recording Statute relating to chattel mortgages is printed herein as Appendix B, but in summary simply requires the mortgage to be delivered to the office of the county clerk of the county in which the mortgagor resides, or maintains its principal place of business, and requires the clerk of the county court to keep a separate book called a "Chattel Mortgage Minute Book", which is the chattel mortgage index. This Statute recognizes the same statutory scheme of recording chattel mortgages as was carried through in the Uniform Commercial Code without change of substance.

Decisions prior to the adoption of the Uniform Commercial Code, and decisions subsequent to its adoption, but relating to documents executed prior to the adoption of the Code, uniformly held that a mineral lessor's lease was valid and superior to the claims of

chattels placed upon the leasehold, unless the chattel mortgage was recorded prior to the placing of the chattels upon the leased premises and without reference to or requirement of recording of a mineral lease both as an instrument affecting realty, and as an instrument affecting chattels.

Illustrative of these cases are:

Norton Coal Corporation v. Maddox (1965), 391 S.W. 2d 386, held the contractual lien of the lessor superior to a chattel interest in equipment subsequently placed upon the leasehold.

North Star Company v. Howard (1960), 341 S.W. 2d 251, recognizing the superiority of the landlord's lease lien over claims of others to chattels on the leased premises, but also holding that the contractual lease lien was not superior, in one instance to a chattel mortgage, where the coal lease was not recorded in the county clerk's office of the county where the principal place of business of the lessee-mortgagor was located. This decision clearly and unequivocally illustrates the basic philosophy of the Kentucky Legislature and Court that *an instrument is notice when lodged for record in the proper office.*

It is the lodging in the proper office that counts, not the corner of the office in which it is deposited by the recording officer.

Of like import is Frick & Lindsay Co. v. Beard, (1925), 211 Ky. 536, 277 S.W. 836, where a combination document, constituting a contract of sale, (recordable on the deed books), and also granting a lien on the property to secure indebtedness was held by the Kentucky Court to be notice, saying—

"Beard was not responsible that the clerk did not record the paper on the mortgage book. He delivered the paper to the clerk for record; the clerk recorded it on the deed book. This was not Beard's fault."

As there are no substantial differences in the statutory scheme for recording instruments affecting chattels prior to the adoption of the Uniform Commercial Code and the requirements of that Code, the decision of the Court of Appeals, constitutes a material and unwarranted departure from the settled law of this State, to the serious detriment of the petitioners.

CONCLUSION

For the foregoing reasons, this Petition for a Writ of Certiorari should be granted.

Respectfully submitted,

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APPENDIX "A"

No. 18363

UNITED STATES COURT OF APPEALS

FOR THE SIXTH CIRCUIT

IN THE MATTER OF:
LECKIE FREEBURN COAL COMPANY - - - *Bankrupt*

OCTAVIA FOSTER, BILLY HOWARD SMITH,
CLYDE HEFLIN, Trustee, ETHEL SMITH,
and JUDY PORTER - - - - - - - *Appellants*

v.

WILLARD M. HAMBLIN, Trustee in
Bankruptcy - - - - - - - - - - *Appellee*

ON APPEAL from the United States District Court for the Eastern District of Kentucky.

Decided January 29, 1969.

Before: CELEBREZZE, PECK and MCCREE, Circuit Judges.

CELEBREZZE, Circuit Judge. This appeal comes to us from a judgment of the United States District Court for the Eastern District of Kentucky affirming the findings of fact and law of the Referee in Bankruptcy. Octavia O. Foster, Billy Howard Smith, Clyde Heflin,

Trustee, Ethel Smith and Judy Porter, hereinafter Appellants, aver that their security interest in the bankrupt's mining machinery and equipment has priority over the lien arising under Section 70(c) of the Bankruptcy Act, 11 U.S.C. § 110(c) in favor of Willard M. Hamblin, Trustee in Bankruptcy, hereinafter Appellee.

In a lease dated August 1, 1961, Leckie Freeburn Coal Company, Inc., hereinafter the Bankrupt, was granted the right to mine coal from 3,623.80 acres of land on the waters of the Johns Creek and Polk Creek in Pike County, Kentucky for a period of twenty years. The lease was filed in the Pike County, Kentucky Clerk's office. It was recorded in Deed Book 421, page 580 at that office on October 20, 1961 pursuant to KRS 382.080; KRS 382.110. The lease agreement was indexed as required under KRS 382.200. There was no separate instrument filed as a financing statement, pursuant to KRS 355.9-302, KRS 355.9-401, and KRS 355.9-402.[1]

Leckie Freeburn Coal Company mined coal on the premises until late in 1965 when it went bankrupt. At the time of its filing a petition for voluntary bankruptcy on January 14, 1966, there was no question but that the Bankrupt owed Appellant lessors $43,283.14 which included royalties accruing under the lease—plus a sum for taxes which the bankrupt lessee was obligated to pay.

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[1] The Uniform Commercial Code sets out the formal requisites of a financing statement and also a form which may be used. KRS 355.9-402. However, a security agreement (or another instrument) which satisfies the formal requisites of KRS 355.9-402 may be filed as a financing statement.

Appellants are claiming a lien upon the mining machinery and equipment of the Bankrupt under Paragraph 17 of the lease agreement which provides as follows:

> "It is further understood that the Lessee expects to acquire the tipple and preparation plant used by said former operator and to use the same together with other mining machinery and equipment owned by the Lessee in its operations hereunder; and it is agreed that said tipple, preparation plant and all of Lessee's mining machinery and equipment upon said premises shall be subject to a lien to secure unto Lessors payment of all rental and royalties which shall have become due and payable hereunder, and Lessors, their successors, heirs or assigns may enforce such lien by distress or otherwise as may be provided by the laws of Kentucky now or hereafter in force and effect. . . . ."

The mining machinery and equipment which was located on the premises of Appellants and owned by the Bankrupt has been sold by the Trustee pursuant to a court order. Appellants now assert a lien upon the proceeds. It is their contention that the lease as filed in the Clerk's office complied with the Uniform Commercial Code. Therefore, Appellants' security interest would be superior to that of the Trustee in Bankruptcy.

Although the Uniform Commercial Code was adopted in Kentucky in 1958, it did not become effective until July 1, 1960. KRS 355.1-101. Since the effective date is prior to the filing of the instrument, both the filing and instrument would have to comply with the Uniform Commercial Code in order to create

a security interest in the personalty which would be superior to the lien of the Trustee. It remains undisputed that the security agreement is governed by the Uniform Commercial Code.

The Uniform Commercial Code as adopted in Kentucky changed the concept of security transactions. The purpose is to uniformly regulate security devices concerning personal property and fixtures. KRS 355.9-102. It prescribes the proper and necessary methods for the perfection of a security interest against third parties. KRS 355.9-402.

The issue before this Court is whether the filing and subsequent recording of the lease agreement in the real estate Deed Book in the office of the County Clerk of Pike County, Kentucky, is sufficient under the Uniform Commercial Code to perfect a security interest in favor of the lessors [Appellants] on the mining machinery and equipment of the Bankrupt.

It is clear on the face of the instrument that the parties intended to create a non-possessory security interest. Since the security interest was created in personal property, it is governed by the Uniform Commercial Code. KRS 355.9-102; KRS 355.9-104; KRS 382.200(2). In order to perfect such a security interest under the facts of this case the Uniform Commercial Code requires the filing of a financial statement pursuant to Part 4 of Article 9, KRS 355.9-401 to 406 and KRS 355.9-302. If it were unperfected at the time of the filing of the petition for bankruptcy, the Trustee's lien would have priority over it. KRS 355.9-301(1)(b); KRS 355.9-301(3). See *In The Matter of Luckenbill,* 156 F. Supp. 129, 130 (1957).

Appellants contend that their filing of the lease with the Clerk of Pike County was in substantial compliance with KRS 355.9-401 requiring the filing of a financial statement with the Clerk of Pike County in order to perfect its lien. KRS 355.9-302.

This Court is of the opinion that the filing of the lease with the Clerk and its proper recordation in the Deed Book does not effectuate a perfected security interest in the personalty in compliance with the Uniform Commercial Code. This Court is cognizant of the long line of property cases cited by Appellants which seem contrary to this Court's position, but also notes that none of them relate to decisions under the Uniform Commercial Code.

It is true that the proper Clerk did receive the instrument for filing under either KRS 382.110 or KRS 355.9-401. However, this was not sufficient to comply with the Uniform Commercial Code. When one takes into consideration (1) that KRS 382.200 which provides for cross indexing of instruments filed under KRS 382.110 refers those filing chattel mortgages, financing statements or security agreements to KRS 355.9-403 and (2) that separate fees exist for each type of filing, more is required of the filing party than to just hand the instrument to the Clerk. KRS 64.010. When dealing with a multi-purpose document, it is incumbent upon the filing party to disclose to the Clerk the purpose for recording. In the present case the record does not show that Appellants had directed the Clerk to record the lease as a financing statement when they paid the filing fee. Had specific directions been proved, this Court would be faced with a different

situation. Here we are not faced with the problem of an improper recording.

Appellants further contend that the lease as recorded in the Deed Book is constructive notice to all, not only as to the lease agreement, but also as to the security interest created therein. Their theory is based upon cases dealing with an improper recording. *Great Western Petroleum Company* v. *Sampson,* 192 Ky. 814, 234 S.W. 727. To allow constructive notice in this case would defeat the purposes of the recording statutes. One object of filing a financial statement is to insure a bona fide purchaser that his title will not be encumbered. For the Court to hold that the filing of this instrument as a lease provided constructive notice to those searching the records for a financing statement would be wholly illogical. *In Re King Furniture City, Inc.,* D.C. Ark. 1965, 240 F. Supp. 453; *Henry* v. *Louisville Rolling Mill Co.,* 7 Ky. Op. 295 (1873). It is the opinion of this Court that it is implicit in the Kentucky statutory scheme that if a party intends a single document to serve multiple purposes and where each purpose requires recording to effectuate its validity, duplicate instruments must be supplied and the Clerk must be informed as to the purpose for which each is to be recorded. See Bender's Uniform Commercial Code Service, Section 16.05. This Court is in agreement with the District Court in upholding the decision of the Referee in Bankruptcy.

Appellee contends that since the lease purported to create a security interest in after-acquired property and granted the Bankrupt the power to sell the

collateral, the lease would be void under a long line of Kentucky decisions decided prior to the effective date of the Uniform Commercial Code. *Phelps* v. *Turner,* Ky., 351 S.W. 2d 176 (1961); *Scoggan* v. *Dillon,* Ky., 252 S.W. 2d 35 (1952); *Sandy Valley Grocery Co.* v. *Patrick,* 276 Ky. 768, 103 S.W. 2d 307 (1937).

In the *Scoggan* case, supra, the Court stated, in affirming *Sandy Valley Grocery Co.* v. *Patrick,* supra, that:

> "the Court [in Sandy Valley] was reluctantly driven to a contrary conclusion under the doctrine of stare decisis and held that such a line on stock of merchandise was invalid as against creditors who became such after its execution and did not entitle the mortgagee to preference to proceeds in the hands of a receiver."

However, in the later decision although still governed by the law prior to the adoption of the Uniform Commercial Code in Kentucky, the Court in *Phelps* v. *Turner,* supra, was also reluctant and belabored with the problem of once again affirming the Common Law doctrine that mortgages were illegal on after-acquired property, especially where the debtor had exclusive control. The Court was heartened by the knowledge that the Uniform Commercial Code would change the existing law. KRS 355.9-204; KRS 355.9-205. The Court stated:

> "We affirm the judgment on the basis of the Sandy Valley Case, *comforted* by the knowledge that the Uniform Commercial Code, KRS 355.9-204, now effective in this jurisdiction, permits mortgages on after-acquired goods." (Emphasis added.)

Lastly, Appellants contend that the Uniform Commercial Code excludes this lien from its coverage under KRS 355.9-104(b). The Referee was correct in his interpretation that this Section of the Code was referring to liens created by statute, e.g., "Mechanics' Liens, Materialmen's Liens", etc., and not to a lien created by contract. *In Re King Furniture City, Inc.*, D.C. Ark. 1965, 240 F. Supp. 453.

Affirmed.

APPENDIX "B"

ENCUMBRANCES

382.670 [523b-8] **Recording of chattel mortgages.** (1) Chattel mortgages, in order to be recorded, shall be filed in the county where the mortgagor if a resident of the state, resides at the time of the execution thereof. If the mortgagor is not a resident of the state, the mortgage shall be filed in the county where the mortgaged property is located at the time of the execution of the mortgage. In the case of a mortgage executed by more than one mortgagor, the filing shall be in each county where the resident mortgagors reside, and if any of such mortgagors are not residents of the state, then also in the county where the mortgaged property is located at the time of the execution of the mortgage.

(2) Chattel mortgages shall not be recorded at length, but, upon filing them in the office of the county clerk, all persons shall thereby be charged with notice thereon and of the rights of the mortgagee, trustee, his or its assigns or representative thereunder.

(3) The county clerk shall keep a separate book called a "chattel mortgage minute book" in which he shall enter an abstract of all chattel mortgages filed with him. This book shall be ruled off in separate columns, with heads as follows: Time of filing, name of mortgagor, name of mortgagee or trustee, date of instrument, amount secured thereby, when due, property mortgaged or pledged, and remarks. The proper entry shall be made under each head, immediately upon the filing of the instrument.

(4) Under the head of "property mortgaged" it shall be sufficient to enter a general description of the property, and an index shall be kept in the manner as required for pledges and mortgages of real property.

(5) The county clerk shall mark the original instrument filed with the time thereof and the number and page of the book where the abstract thereof may be found, and the instrument shall be preserved as a public record of his office, filed and indexed in regular alphabetical order so as to be readily accessible for inspection.

(6) When recorded chattel mortgages are fully satisfied and paid, the county clerk shall deliver the original instrument and any other instrument filed, acknowledging full satisfaction thereof, to the mortgagor or his assigns. Such delivery may be made by placing such instrument in United States mail, postage prepaid, directed to the last known address of the mortgagor or his assigns or representatives.

(7) At the time of filing of any chattel mortgage the county clerk shall, upon request, issue to the person filing it a receipt in writing which shall contain the names of the parties to the mortgage, its date, amount, number and the time of its filing.